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UNCLAS SECTION 01 OF 02 RANGOON 001139

SIPDIS

SENSITIVE

STATE FOR EAP/MLS, EB/TPP
TREASURY FOR OASIA:AJEWELL

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SUBJECT: BURMESE KYAT DEPRECIATES TO RECORD LOW

Refs: Rangoon A)1073, B)0924, C)0542, D)0489

1. (SBU) Summary: The unofficial rate of the Burmese kyat reached a record low of K.1360/\$1 on September 30, beating the previous record of K.1270/\$1 in September 2002. This depreciation reflects the worsening economic situation, and may continue until at least Nov/Dec, when the kyat traditionally appreciates as new crops of opium poppy and tourists come in. End summary.

Depreciation Momentum Builds

2. (SBU) One year ago, the rate was K.932/\$1. The rapid 46% decline started after the bomb explosions in Mandalay and Rangoon on April 26 and May 7 (refs C, D). Shortly thereafter, at a May 15 press conference, the deputy finance minister indirectly warned people to handle foreign currencies only according to official regulations, which preclude exchanging at the commonly-used unofficial rate. He also cited the seizure of \$90,000 from a local resident at the Rangoon airport. (Note: It is technically illegal for Burmese citizens to hold foreign currency without official permit. End note.) His statements sparked worries about a possible scarcity of dollars, and pushed the exchange rate up to K.1010/\$1 on May 24. Cyclical forces also affect the rate: the kyat usually falls from May to November (rainy season) and appreciates from December to April (tourist and harvest season).

3. (SBU) The kyat's unofficial rate of K.1360/\$1 in September is the record low in Burma's market exchange rate history. The official rate remains fixed at K.6/\$1, as it has for the last two decades, but this rate is used only for recording import/export transactions in the government's imaginary budget. There are numerous reasons for the recent plunge, including:

-- The government took control of a private bank, the Myanmar Universal Bank (MUB), in early August without any official announcement (Ref B). This prompted widespread kyat withdrawals from MUB and other private banks, which were then converted into dollars and gold.

-- Rumors about counterfeit K.1000 notes and reports of counterfeit currency seizures further reduced confidence in the kyat.

-- Central Bank financing of the growing budget deficit (K.680 billion, or over \$700 million in 2004-05) creates inflationary pressure.

-- New unpublished trade regulations controlling exports and imports that were introduced in August (ref A) slowed trade and drove some businessmen to increase speculation in local foreign exchange market.

-- Revaluation of the Chinese yuan weakened the Burmese kyat. Also, some traders are now purchasing and holding dollars until they need yuan to counter the daily depreciation they would suffer by holding kyat.

-- Overall mismanagement of the economy by the government and the unpredictable political situation.

Prices Reflect New Rates

4. (U) In the past, when exchange rate and gold prices increased, Military Intelligence (MI) arrested moneychangers and gold merchants, basically halting the unofficial trade for a while. This time there has been no confirmed news of action against moneychangers or gold merchants, although the rates are at record highs. Primarily due to the exchange rate, prices of most imported goods rose from 5% to 20% in September. Some electronic goods and computer stores are now selling goods based on the daily dollar exchange rate.

5. (U) Prices of some locally produced items produced with imported inputs, including detergent powders, coffee mix and medicines, also increased 15% to 20% last month. Taking advantage of the situation, and to help cover other costs, some shopkeepers also raised prices for locally-made goods

(including the staple breakfast fish soup, mokinga). Consumers are told that the high prices are due to the dollar exchange rate. To date, there has been no government reaction.

Comment: Rebound Expected

16. (SBU) Although some think the exchange rate will deteriorate even further before turning around, the end of the rainy season is expected to bring more dollars, and business, into the country. Opium production is down, so the seasonal impact of the poppy harvest may be lower than in previous years. The government is hoping for increased numbers of tourists this season. Their dollars will be welcomed by both residents and government alike. End comment.
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